

Message Text

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ACTION COME-00

INFO OCT-01 NEA-10 ISO-00 EB-11 SS-20 FAA-00 CIAE-00

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FM AMEMBASSY JIDDA

TO SECSTATE WASHDC PRIORITY 5656

INFO AMCONSUL DHAHRAN

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LIMITED OFFICIAL USE JIDDA 5457

E.O. 11652: N/A

TAGS: EMEP, SA

SUBJ: MAJOR PROJECT: NEW JIDDA AIRPORT

REF: STATE 240269

1. EMBOFF PARTICIPATED DEC 9 IN LONG DISCUSSION ON ESCALATION CLAUSE FOR CONTRACT WITH NASSIEF AND A U.S. CORPS OF ENGINEERS CONTRACT EXPERT. (NASSIEF HAS LONG HISTORY OF CLOSE WORKING RELATIONSHIP WITH COE PERSONNEL AND PUTS MUCH STORE ON THEIR JUDGEMENT.)

2. EVIDENTLY DECISION TO INTRODUCE ESCALATION CLAUSE IS NOT YET OFFICIAL, ALTHOUGH ALMOST CERTAIN. NASSIEF'S PROBLEM AT THE MEMENT IS TO DETERMINE HOW ESCALATION CLAUSE SHOULD BE STRUCTURED. COE OFFICIAL DESCRIBED SYSTEM HE HAD JUST STUDIED IN ITALY: IN BRIEF, CONTRACTOR BEGINS BY BREAKING TOTAL BID INTO MAJOR COST COMPONENTS, E.G. LABOR, CEMENT, STEEL, ETC. ON PERCENTAGE BASIS. THEREAFTER TIME-AVERAGED CHANGES IN PRICE INDICES FOR COMPONENTS ARE APPLIED ACCORDING TO WEIGHTS ESTABLISHED BY ORIGINAL COMPONENT COST BREAKDOWN AND CONTRACT PAYMENTS ADJUSTED ACCORDINGLY WITHOUT ATTEMPTING TO AUDIT CONTRACTOR'S ACTUAL COSTS. ESCALATION PAYMENTS ARE SUBJECT TO A "DEDUCTIBLE" OF A FIXED PERCENTAGE (SAY SIX PERCENT) OF TOTAL ORIGINAL CONTRACT VALUE.

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3. MAJOR DIFFICULTY FOR AIRPORT CONTRACT WOULD BE WHAT TO USE FOR PRICE INDICES. AS SUCH STATISTICS SIMPLY DO NOT EXIST FOR LOCAL MARKET, THERE IS STRONG POSSIBILITY THAT NASSIEF MAY RECOMMEND ARBITRARY ADOPTION OF U.S. CONSTRUCTION MATERIALS COMPONENT INDICES, IF RPT IF USG CAN GUARANTEE TO PROVIDE THEM ON TIMELY MONTHLY BASIS. IN THE ABSTRACT--CONSIDERING THE LOWER INFLATION RATE IN U.S. COMPARED TO EUROPE--THIS WOULD SEEM A GOOD THING. EUROPEAN COMPETITORS WOULD BE FACED WITH CHOICE OF EITHER KEEPING LARGER FUDGE FACTOR IN BID AGAINST UNCOMPENSATED PORTION OF PRICE INCREASES, OR ELSE GREATER RELIANCE ON U.S. MATERIALS/EQUIPMENT. HOWEVER THERE MAY BE OTHER COMPLICATING FACTORS, INCLUDING THE PROPORTION OF NON-US PROCUREMENT NECESSARY FOR EVEN A U.S. CONTRACTOR.

4. ABOVE MAY NOT NECESSARILY BE SYSTEM OF ESCALATION CLAUSE ADOPTED. NASSIEF IS OBVIOUSLY STILL FEELING HIS WAY. HE IS CONVINCED (AND HAS CONVINCED MINISTER OF FINANCE) OF NEED FOR ESCALATION CLAUSE, BUT IS AFRAID OF BEING MOUSETRAPPED INTO SOMETHING EITHER TOO IMPRACTICAL TO ADMINISTER OR GIVING TOO MUCH LEEWAY TO CONTRACTOR. ALSO DISCUSSED WAS IDEA OF NEGOTIATING ESCALATION AGREEMENT WITH ONE OR SEVERAL OF LOWER BIDDERS AFTER BIDS OPENED. ONE SPECIFIC LEFT UNCOVERED WAS LOCAL LABOR COSTS. NASSIEF FELT LOCAL LABOR TOO SMALL AN ELEMENT IN TOTAL COST TO BE WORTH WORRYING ABOUT.

5. HAVE REPORTED ABOVE IN DETAIL ON ASSUMPTION IT WILL BE OF CONSIDERABLE INTEREST TO BROWN AND ROOT. IF B&R LIKE ITALINA OR SIMILAR ESCALATION CLAUSE SYSTEM(WE CAN DE*CRIBE IN GREATER DETAIL IF NEEDED), REQUEST WE BE PROVIDED ASAP WITH SAMPLE MONTHLY PRICE INDICES OVER PAST YEAR ON TYPICAL INPUTS SUCH AS CEMENT, CONSTRUCTION STEEL, HEAVY EQUIPMENT RENTALS, WHICH WE CAN USE AS ILLUSTRATIONS FOR NASSIEF. IF B&R PREFER SOME OTHER SYSTEM, URGE THEY GET IT BEFORE NASSIEF SOONEST. EMBASSY WOULD BE PLEASED TO PRESENT IT TO NASSIEF IN GUISE OF AMICUS CURIAE, UNLESS B&R PREFER TO KEEP IT AS PART OF INDIVIDUAL PACKAGE DEAL.
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